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TAGS: [ECON](#) [PGOV](#) [EINV](#) [AJ](#) [RU](#) [IR](#)  
SUBJECT: REVOLUTION IN THE REVOLUTION: UNDERSTANDING IRAN'S  
PRIVATIZATION JUNGLE

REF: A. A) ASHGABAT 50  
[1](#)B. B) ANKARA 35  
[1](#)C. C) 2009 BAKU 763  
[1](#)D. D) 2009 ISTANBUL 367  
[1](#)E. E) 2009 BAKU 80  
[1](#)F. F) 2009 DUBAI 541  
[1](#)G. G) 2009 DUBAI 409  
[1](#)H. H) 2009 DUBAI 394

Classified By: PolEcon Chief Rob Garverick, Reasons 1.4 (b and d)

#### Summary -----

[1](#)1. (C) Iran has one of the largest state-owned sectors in the world, and privatization has long been an official part of state policy. This "View from Baku" report examines the reality behind Iran's recent privatization effort, based on a wide variety of Baku Iran watcher discussions with Iranian economists, business people, journalists, and bankers as well as some knowledgeable third-country sources.

[1](#)2. (S) The report argues that Iran's privatization program lacks a meaningful domestic constituency, and is better understood as a competitive redistribution of economic power and related political leverage among regime factions, with Revolutionary Guard and Basij elements notionally associated with President Ahmedinejad recently shunting aside other groups. Viewed in Iran's larger economic and political context, privatization developments may also be understood as part of a larger attempt at consolidation of a new ruling class of factional loyalists as an Iranian nomenklatura. End Summary.

#### Iran's Privatization Riddle -----

[1](#)3. (SBU) In 2008, Iran's industrial sector was over 80 percent state-owned. In contrast, the same figure for "communist" China's state-owned sector is 55 percent. Interlocutors and other sources depict these state-owned companies as bloated, inefficient, and top-to-bottom havens for political patronage.

[1](#)4. (SBU) Beginning with the Presidency of Hashemi Rafsanjani (1989-1997), complete or partial privatization of much of the state-owned sector has been an official government goal, and in 2004 Article 44 of the Iranian Constitution was explicitly amended to call for widespread privatization of state industries, and several large state companies have gone

through or are going through a process of privatization. Despite these activities, in September, 2009 the President of the Iranian Chamber of Commerce characterized the Iranian government's privatization program as "a farce" masking a shuffle among state actors. This cable examines this issue, summarizes its logic, and places it in the larger context of ongoing political power competition among regime factions, and prospective evolution of a new ruling class "nomenklatura."

#### Why "Real" Privatization Fails

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¶5. (C) The short answer is that genuine market-or economic-oriented privatization is not occurring because almost no one particularly wants it to. In that sense, it a mistake to call the Iranian privatization program a "failure." This is not solely a matter of the value of the spoils at stake. Reftels, Baku contacts, and other sources concur in presenting the impression that the Iranian privatization as currently pursued is increasingly accomplishing, if somewhat awkwardly, ot economic liberalization, but its opposite - higher concentration of economic and political power in quasi-state/regime faction hands.

¶6. (C) Baku Iranian contacts almost universally concur that current privatization practices, as well as much other state-sponsored economic activity, reflect an effort on the part of regime figures to place potentially high-employment/patronage, profitable, and/or otherwise sensitive assets in the hands of themselves and their allies.

According to this view, the major complicating factors in this process are not economic, but ideological and political, as differing regime factions maneuver for influence and advantage, and watch each other jealously over new divisions of the pie.

#### Iran's Privatization Allergy

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¶7. (C) Despite publicized fiddling with initiatives developed by (powerless) technocrats, revised investment laws, and massive official rhetoric endorsing privatization and investor-friendly goals, genuine privatization lacks a significant government or other political constituency in Iran. In fact, except for some economists, bankers, and entrepreneurs, a contrary attitude prevails. Several interlocutors agreed that, in much of the popular mind, privatization of large industries and related foreign investment equal exploitation, and "giving our resources away to foreigners." In contrast, they asserted, state ownership connotes protection of national interest, economic subsidies and plentiful (and often make-work) jobs to hand out to needy citizens, including veterans and system political/faction supporters and their clans.

¶8. (C) An Iranian banker who personally favors privatization conceded that "it is hard to overcome the weight of our history (of foreign exploitation), and our intelligentsia's addiction to Socialist thinking." A pro-liberalization economist noted that on privatization "our spectrum of opinion basically runs from Left to Left." A former Iranian magazine editor agreed, arguing that a "massive public relations campaign will be needed to change the public's (negative) attitude."

#### No Foreigners, Please

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¶9. (C) In public, Iran's privatization program is often associated by the government and outside observers with efforts to increase foreign investment. Contacts report that while foreign (and domestic) investment is officially encouraged, in practice would-be investors are often blocked from investing in large, remotely strategic, and/or profit-making industries. In a typical example, the Iran

agent for the largest Russian steel company, Magnitogorsk Steel, was "waived away" by regime authorities from pursuing an effort to take a 25 percent stake in the Isfahan steel works, though originally encouraged to do so by Isfahan steels' management.

¶10. (C) There are also complaints about the post-purchase experiences of private entrepreneurs and investors who managed to acquire small-to-medium sized privatized facilities. An Iranian businessman contended that, despite what the official privatization rules say, "it is impossible for all but the most (regime)connected private owners to fire unproductive people" working at privatized facilities. The owner of a textile factory privatized in 2005 claimed that it remains stuffed with excess and unproductive workers, whom he is unable to fire (despite his legal right to do so) due to political and security service interference and intimidation. He complained that he wanted to give back the facility or give it to the workers due to constant outside interference, but was "not being to do that" to by the authorities. He added however that the plant could be very profitable, "if modernized and properly run." He speculated that he will eventually hand over the facility to someone better connected.

#### Reshuffling the State-Owned Deck

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¶11. (C) If classic commercial privatization is not happening, then what is? Interlocutors characterized most of the current privatization going on in Iran today as an insider's game masking a shuffling of the deck between state Ministries; para-statals (including pension funds and insurance companies) controlled by regime insiders; regime-connected clerical foundations ("Bonyads"); and Revolutionary Guard/Basij front companies, which are reportedly are increasingly expanding their relative economic position at the expense of the preceding groups.

Before: Rafsanjani, Larijanis, and Ali Khamenei

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¶12. (S) The former head of one of Iran's largest credit unions, a one-time Hashemi Rafsanjani assistant (strictly protect), asserted that at least until recently, three actors carried the greatest weight in dominating Iran's reshuffling of the privatization deck: Rafsanjani, the family of (current Majlis Speaker) Ali Larijani, and Supreme Leader Ali Khamenei, whom he said "works through the Forty-Third Office of the Intelligence Ministry." He described the latter office as a semi-secret body closely linked to Khamenei that coordinates Iranian government strategies.

Now: Revolutionary Guard/Basij Factions On Top?

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¶13. (S) Dividing state spoils is nothing new, either in Iran or elsewhere. However, since late 2008 Iran watcher has heard more and more reports suggesting that an important regime shift may be underway in this area, rejecting earlier balancing acts by favoring Revolutionary Guard, Basij, and "Ahmedinejad/Mesbah-Yazdi factions" at the expense of other insider groups. Whatever the truth, aggressive expansion of this group into commercial areas has noticeably gathered speed, especially since June, 2009 (refs a-d).

¶14. (S) Though the overall situation remains unclear, the recent murky "privatization" of the state telecommunications company, in which all non-Revolutionary Guard/Basij companies were blocked from participating (see ref h), issuance of new banking licenses to Revolutionary Guard fronts, and recent reports of plans to transfer the Iran Khodro auto company, Isfahan Steel, major mines, and railroad construction projects to other Revolutionary Guard entities (reftels) lend credence to this alleged trend.

¶15. (S) Recent rumors that Rafsanjani associates are being dislodged from control of oil production infrastructure in favor of Revolutionary Guard and/or Ahmedinejad supporters

would be further evidence, if confirmed. Motivations for taking control over these companies (some loss-making) are presumably varied, and not always crystal clear, but there are no indications as yet that determination to render them objectively more efficient or profitable was necessarily one of them.

Comment - "Revolution in the Revolution?"  
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¶16. (C) In some respects Iran's current privatization practices resemble a slow-motion version of the insider, oligarchic scramble for control over Russia's state-owned industrial assets after the collapse of the Soviet Union. However, there are important differences. The post-Soviet grab was for a handful's access to money, while recent privatization trends in Iran more explicitly buttress a contest among specific regime factions over domination of Iranian society. Related measures include expanded control over employment opportunities, more restrictive access to large contracts, increased university quotas favoring presumed supporters, tighter control over security services, increased Revolutionary Guard/Basij crony presence in the agricultural sector (septel); and other measures. If true, this is a seminal event, on par with the Iranian government's extensive loss of credibility and galvanizing of opposition elements following the stolen June, 2009 presidential election.

¶17. (C) Largely left out of the process are economic technocrats; urban business, management, and technical professionals; and the majority of the educated and middle classes. Most Iranian sources suggest that a new political-economic system is being created that will benefit approximately ten percent of the population, while disadvantaging (or scarcely affecting) the balance of the population. These potential beneficiaries consist primarily of established regime insiders and their relatives/cronies; Revolutionary Guard and Basij personnel and family members; and some ideologically-correct working class veterans of the Iran-Iraq war and their children who belong to patronage networks. If events proceed unchecked, these may with some

intent become the underpinnings of the new Iranian nomenklatura.

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